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February 14, 1997

VIA HAND DELIVERY

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
1919 M Street, N.W., Room 222
Washington, D.C. 20554

Re: Reply Comments of Telco Communications Group, Inc. Submitted in Response to the FCC's Notice of Proposed Rulemaking in the Matter of Access Charge Reform, CC Docket No. 96-262

Dear Mr. Caton:

Enclosed for filing, please find an original and sixteen (16) copies of the Reply Comments of Telco Communications Group, Inc. in the above-referenced docket.

Also enclosed is a diskette copy of this filing. If you have any questions, please do not hesitate to call me at (202) 945-6917.

Sincerely,

Tamar E. Haverty

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WASHINGTON, D.C. 20007-5116

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Access Charge Reform	)	CC Docket No. 96-262
	)	
Price Cap Performance Review for Local Exchange Carriers	)	CC Docket No. 94-1
	)	
Transport Rate Structure and Pricing	)	CC Docket No. 91-213
	)	
Usage of the Public Switched Network by Information Service and Internet Access Providers	)	CC Docket No. 96-263

REPLY COMMENTS OF TELCO COMMUNICATIONS GROUP, INC.

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In the Matter of	)	
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REPLY COMMENTS OF TELCO COMMUNICATIONS GROUP, INC.

Telco Communications Group, Inc. and its subsidiaries Dial & Save and Long Distance Wholesale Club (together "Telco"), by undersigned counsel and pursuant to the Federal Communications Commission's ("FCC") Notice of Proposed Rulemaking issued in the above-captioned proceeding[1] (released December 24, 1996), hereby submit the following Reply Comments.

[1] *In the Matter of Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, and Usage of the Public Switched Network by Information Service and Internet Access Providers*, FCC 96-488, CC Docket Nos. 96-262, 94-1, 91-213, and 96-263, Notice of Proposed Rulemaking, Third Report and Order, and Notice of Inquiry (rel. Dec. 24, 1996) ("Notice" or "NPRM").

Introduction and Summary

In its initial Comments on the FCC's Notice, Telco urged the FCC to adopt a prescriptive approach to access charge reform and reduce access charges to cost-based rates as soon as possible. Although the Regional Bell Operating Companies ("RBOCs") and other independent local exchange carriers ("LECs") predictably disagreed, most other parties overwhelmingly favored the adoption of a prescriptive approach. As Telco and others argued, there is not enough evidence to support the theory that, at this time, competition will drive access charges to cost-based or market rates. Numerous parties, including state regulatory commissions, presented evidence of the lack of competition in the local exchange and exchange access markets. Although competitive market forces might help drive access charges to costs at some time in the future, the FCC cannot rely on market forces now and must move quickly to reduce access charges to cost.

Telco also urged the FCC to reduce market distortions created by regulatory policies by (1) directing the States to adopt intrastate access charges that are substantially similar to interstate rates and (2) basing access charges on the same pricing standards adopted for the purchase of interconnection, unbundled network elements, and collocation. Again, many parties submitting comments in this proceeding supported Telco's position that access charges should be based on some form of total element long run incremental cost ("TELRIC") or total service long run incremental cost ("TSLRIC"). The FCC must not be dissuaded from adopting TELRIC or TSLRIC pricing by the RBOCs' and independent LECs' unsubstantiated cries of "takings."

I. The FCC Should Adopt a Prescriptive Approach to Access Reform and Quickly Reduce Access Charges to Costs.

Parties overwhelmingly favored the adoption of a prescriptive approach to access reform. For example, the Missouri Public Service Commission, arguing that effective competitive market forces do not yet exist, urged the FCC to adopt a prescriptive approach:

> A full year after the Act, only the first few competitors have actually begun operation. It may well be another year before any significant competition develops beyond these first tentative steps. ... It is unclear how long it will take before competition could or will develop to the extent that competitive forces can be relied upon to bring access rates in line with access costs, but in some locations it may be years before this occurs.[2]

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[2]Missouri Public Service Commission ("Missouri PSC") Comments at 4. *See also*, Tennessee Regulatory Authority Staff ("Tennessee Staff") Comments at 4 (prescriptive rates appropriate until an area is deemed competitive); Washington Utilities and Transportation Commission ("Washington UTC") Comments at 7-8 (advocates use of prescriptive methods until sufficient competition exists in local markets; sufficient competitive forces do not exist in the State of Washington); Texas Public Utilities Commission ("Texas PUC") Comments at 23-24 (competition in local exchange markets is not yet present in Texas; advocates use of a prescriptive approach initially with transition to a market-based approach when true competition exists); Florida Public Service Commission ("Florida PSC") Comments at 3 (recommends prescriptive approach); District of Columbia Public Service Commission ("DC PSC") Comments at 2-3 (continue use of prescriptive rules as an interim measure until there is evidence that actual competition has developed); AT&T Comments at 15 (neither the prospect of unbundled network elements at TELRIC-based rates nor the more distant prospect of facilities-based competition currently constrains incumbents' access prices); Competitive Telecommunications Association ("CompTel") Comments at 13 (access rates will not move to TSLRIC absent a prescriptive approach); Sprint Comments at 37 (there is virtually no local service competition today); MCI Comments at 33 (using a market based approach in a market that remains a virtual monopoly is destined to fail); IXC Long Distance ("IXCLD") Comments at 4 (recommends prescriptive approach until incumbents empirically prove the existence of a truly competitive local exchange market); Excel Comments at 7 (recommends prescriptive approach); Telecommunications Resellers Association ("TRA") Comments at 18 (recommends prescriptive approach).

Contrary to incumbent LECs' arguments, the existence of state-approved interconnection agreements or a statement of generally available terms and conditions ("SGAT") does not create a competitive environment.[3] Until competitors actually order and combine unbundled network elements (or build their own facilities), to provide exchange access, there will be no competitive pressures placed on incumbent LECs to reduce their inflated access charges.[4] Therefore, *if* the FCC decides to combine the prescriptive and market-based approaches, Telco recommends that it significantly alter its proposed competitive triggers. Regulation of incumbent LECs' access charges should not be relaxed unless and until the incumbent can show that competitors are ordering and

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[3]GTE Service Corp. ("GTE") argued that the existence of unbundled network elements together with approved interconnection agreements will constrain access prices. GTE Comments at 12 (citing its 34 approved agreements in 13 states). GTE's Comments failed to mention, however, that GTE has appealed arbitration decisions in 15 states. *See*, CompTel Comments at 10.

[4]*See*, Florida PSC Comments at 7 (more experience is needed to determine if unbundled network elements are actually used to create viable competitive alternatives); CompTel Comments at 5 (for network elements to provide a viable local entry vehicle, they must be as simple to order, easy to provision, and as responsive to customer demand as switched access has become over the past decade).

MCI provided concrete examples of the difficulties it has encountered in starting up local service on a trial basis in California:

> MCI customers have been told by PACTEL employees that MCI is not legally authorized to provide local service; customers have had their service disconnected before their new MCI local service is connected; customers have been forced to wait as much as six weeks for their new MCI local service to be started by PACTEL, during which time PACTEL has tried to recruit back customers that were waiting to be switched; and PACTEL has failed to take steps to make customer switches electronic and seamless.

MCI Comments at 38.

combining unbundled network elements and providing local exchange service and exchange access using unbundled network elements or a combination of unbundled network elements and their own facilities.[5] In other words, the FCC should not implement any regulatory relief until incumbents have met the Phase 2 trigger proposed by the United States Telephone Association ("USTA")[6] as well as the majority of Phase 1 triggers proposed in the Notice.[7] Furthermore, Telco agrees with the California Public Utilities Commission[8] that the incumbent LEC should be required to show the presence of active competitors by discrete and measurable factors[9] such as the number of cross-connects and number of unbundled loops provisioned.

While reliance on competitive market forces may be preferable to regulation in the long run, Telco agrees with TRA that a prescriptive approach to access charge reform is consistent with the pro-competitive objectives of the 1996 Act[10] and that a more aggressive regulatory posture in the

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[5]*See*, ACC Long Distance Corp. ("ACC") Comments at 8-9 (petitioning incumbent should be required to demonstrate that competitors are ordering and receiving unbundled network elements and physical collocation in a commercially reasonable manner and are able to combine unbundled network elements to provide end-to-end service); ALTS Comments at 7 (no question that expanded interconnection is critical to the creation of effective access competition); DS PSC Comments at 2-3 (competitors should be actually offering services to all segments of a market before the ILECs are freed from controls).

[6]USTA Comments at Attachment 8 (interconnection agreement or effective SGAT **with use** or facilities based provider).

[7]Notice at ¶ 163.

[8]California PUC Comments at 11.

[9]*See also*, ALTS Comments at 2-4 (quantitative market measurements must be employed); IXCLD Comments at 4 (competitive market must be empirically proven).

[10]*Telecommunications Act of 1996*, Pub. L. No. 104-104, 110 Stat. 56 (1996) ("1996 Act").

near term will ultimately allow for more expeditious deregulation in the long run.[11] Telco therefore urges the FCC to adopt a prescriptive approach immediately and transition to a market-based approach only after incumbent LECs meet the competitive triggers outlined above.

II. THE FCC SHOULD NOT GRANT USTA'S FORBEARANCE REQUEST

The FCC should *not* forbear from regulating services in the interexchange basket, special access, collocated direct trunked transport, and directory assistance. The parties advocating forbearance[12] cannot meet the first prong of the forbearance test[13] on a nationwide basis. For example, the presence of competitive alternatives for services such as transport and special access service varies widely by locality:

> California has experienced significant competition for transport services in recent years, but only in particular geographic areas. Only in those areas does hi-capacity access service warrant increased LEC deregulation. California is not convinced that other LEC access services face a similar degree of competition.[14]

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[11]TRA Comments at 18-20.

[12]*See, e.g.*, GTE Comments at 44; Pacific Telesis Group ("PacTel") Comments at 28; Southwestern Bell Telephone Company ("Southwestern Bell") Comments at 19; USTA Comments at 35-48; US West Comments at 42;

[13]The first prong requires a determination by the Commission that "enforcement of such regulation or provision is not necessary to ensure that the charges, practices, classifications, or regulations by, for, or in connection with that telecommunications carrier or telecommunications service are just and reasonable and are not unjustly or unreasonably discriminatory." 47 U.S.C. § 10(a)(1).

[14]California PUC Comments at 10-11. *See also*, Florida PSC Comments at 7.

Sprint also provided evidence showing that alternative access providers have made few inroads in the access market despite their presence in the market for almost a decade.[15] Therefore, forbearance requests for specific services in specific geographic areas would be more appropriately handled in separate proceedings.

III. Access Charges Should Reflect TELRIC and Should Not Be Based on Incumbents' Embedded Costs

As Telco argued in its Comments:

> In order to remove any potential market-distorting incentives regarding a carrier's choice between incumbent LECs' access services and the purchase of unbundled network elements to provide switched access, the FCC must base the prices for access and interconnection on the same standard -- Total Element Long Run Incremental Cost ("TELRIC").[16]

The ability to substitute unbundled network elements for access service will create opportunities for arbitrage if unbundled network elements and access are not priced similarly.[17] Many parties supported the adoption of either the TELRIC or TSLRIC standard to reduce access

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[15]Sprint Comments at 37-38 (alternative access providers received less than nine cents of every special access dollar spent by Sprint in 1996).

[16]Telco Comments at 7.

[17]*See, e.g.*, Southwestern Bell Comments at 4 (interconnection pricing rules have had the practical effect of forcing LECs to price access at the level of unbundled network elements). The California PUC expressed concern about the potential for arbitrage if intrastate and interstate access costing standards differ. California PUC Comments at 13. As Telco suggested in its Comments, the FCC should eliminate this potential opportunity for arbitrage also.

charges to cost.[18] The FCC should base access prices on the same forward-looking cost standard that it has already found just and reasonable for functionally equivalent unbundled network elements.[19]

The FCC should reject incumbent LECs' arguments that adoption of TELRIC or TSLRIC pricing of access charges without a mechanism to allow recovery of incumbents' embedded costs will result in an unconstitutional regulatory taking. In a competitive environment, no firm is guaranteed recovery of its embedded costs. Incumbents cannot be free to respond to competition and be guaranteed a particular level of revenues. Indeed, incumbents subject to price cap regulation have already given up a guaranteed revenue requirement.[20] At this stage of the proceeding (where the FCC is still evaluating numerous proposals to restructure its access charges) it is clearly premature for the FCC to address takings claims now.[21] It begs credulity to allege that all proposed changes included in the Notice would result in an unconstitutional taking of incumbent LECs'

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[18]*See, e.g.,* AT&T Comments at 19 (TELRIC or TSLRIC); California PUC Comments at 9 (TSLRIC plus reasonable share of joint and common costs); CompTel Comments at 17 (TSLRIC); IXCLD Comments at 2-3 (TELRIC); MCI Comments at 18 (TELRIC estimates made by proxy cost models); Sprint Comments at 49-50 (TELRIC); Texas PUC Comments at 27 (TELRIC).

[19]*See*, AT&T Comments at 11-12.

[20]Florida PSC at 10. AT&T argues that most of incumbent LECs' alleged "at risk" investment was undertaken after price cap regulation replaced rate-of-return regulation and that under price cap regulation, there could be no legitimate expectation of guaranteed embedded cost recovery. AT&T Comments at 31-32.

[21]*See*, ALTS Comments at 27 (plainly premature for FCC to address takings claims now in absence of any quantification from incumbent LECs); California PUC Comments at 16 (premature to determine now whether incumbent LECs in competitive areas will not have an opportunity to earn a fair rate of return).

property. Until the net effect of the FCC's Order on incumbent LECs is known, it is impossible to determine whether the Order will result in a taking.[22]

The FCC should also reject incumbent LECs' arguments that they are Constitutionally entitled to recover all of their embedded costs because their investments have been approved by state or federal regulators.[23] The Supreme Court has specifically rejected the prudent investment rule[24] as the Constitutional standard to be applied when evaluating claims of regulatory takings.[25] More recently, the D.C. Circuit rejected a claim by Ameritech that the FCC's discounted cash flow ("DCF") rate of return violated the Fifth Amendment's takings clause:

> Even assuming the DCF rate of return fails to cover the [Regional Holding Companies'] RHCs' losses from the disallowance of prudent investments, Ameritech has not shown that a "used and useful" rate base is unconstitutional. There simply has been no demonstration that the FCC's rate base policy *threatens the financial integrity of the RHCs or otherwise impedes their ability to attract capital.*[26]

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[22]*Duquesne Light Co. v. Barasch*, 488 U.S. 299, 314 (1989) (Constitution protects the utility from the net effect of the rate order on its property); *accord, Illinois Bell Telephone Co. v. FCC*, 988 F.2d 1254, 1263 (D.C. Cir. 1993) (the test to be applied is whether the end result meets the *Hope* standards: attraction of capital and compensation for risk).

[23]*See, e.g.*, GTE Comments at 83 (incumbents must have the opportunity to recover any investment that state or federal regulators allowed at the time the investment was made); Southwestern Bell Comments at 40.

[24]Under the prudent investment rule, the utility is compensated for all prudent investments at their actual cost when made, irrespective of whether individual investments are deemed necessary or beneficial in hindsight. *Duquesne*, 488 U.S. at 299.

[25]*Dusquesne*, 488 U.S. at 315.

[26]*Illinois Bell*, 988 F.2d. at 1263 (emphasis added).

Telco is confident that the FCC is aware of its Constitutional duties and will consider the overall impact of any access charge reform rules adopted in this proceeding. The FCC should not, however, allow vague and unsubstantiated cries of "takings" to dissuade it from adopting pro-competitive rules that are consistent with the FCC's trilogy of actions that "collectively are intended to foster and accelerate the introduction of efficient competition in all telecommunications markets, pursuant to the mandate of the 1996 Act."[27]

Conclusion

Although competitive market forces might help drive access charges to costs at some time in the future, today's "market" for exchange access continues to be dominated by the incumbent LECs. Therefore, at this time, the FCC cannot rely on market forces and must move quickly to reduce access charges to cost.

Respectfully submitted,

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Counsel for Telco Communications Group, Inc.

February 14, 1997

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[27]Notice at ¶ 1.

CERTIFICATE OF SERVICE

I hereby certify that on this 14th day of February, 1997, a copy of the foregoing Comments of Telco Communications Group, Inc. were served via hand delivery on the following:

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Federal Communications Commission
1919 M Street, NW
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Washington, DC 20554

Competitive Pricing Division (2 copies)
Common Carrier Bureau
Federal Communications Commission
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International Transcription Services, Inc. (1 copy)
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